Captive insurance company regulation and oversight is an increasingly scrutinised issue. In most US captive domiciles, captive managers, actuaries providing loss reserve opinions and certified public accountants must apply to be accepted onto approved lists in order to provide services to captives.

These approved lists are similar to, if somewhat less formal than, a state’s licensing of insurance agents, public adjusters, viatical settlement providers and other insurance professionals.

The current environment begs the question: Is the oversight of captive insurance service providers rigorous enough? To gain insight into the regulation of service providers, I asked several regulators the following questions:

- Have you ever removed a captive manager, accountant, or actuary from your approved service provider list?
- If so, how often does this happen?
- Hypothetically, if a court of competent jurisdiction were to make a ruling adverse to a captive service provider on the approved list, would such a ruling be enough for you to initiate action to remove them?
The reality
Let’s start with the basics. Almost all the regulators surveyed had removed at least one captive manager from their state’s approved list. One response indicated the domicile had “removed managers and auditors from our lists”.

Another was more vague, simply stating: “Our list of ‘approved managers’ has shrunk considerably since we started... because they don’t meet the criteria (for) managing a captive.” Other regulators had also removed an auditor and/or an actuary from their approved list, and one expects to remove another in the near future.

A couple of responses ominously added comments such as: “We haven’t had to remove an actuary... yet.”

There was more bad news for actuaries. One response indicated: “While we haven’t removed any actuaries from our list of actuaries approved to provide an opinion on reserves, there are a few that we had consulting contracts with that we didn’t renew.”

All of this feedback appears to support the idea that captive service provider regulation is indeed active.

It starts with the captive
One common theme among the regulators’ responses was that regulation starts with the captive. The response from one domicile indicated they try to avoid difficulties by not licensing problem captives in the first place. Several respondents made this clear by indicating they regulate the captive, not the service providers.

In addition, one regulator noted the ongoing regulation of captives also provides valuable information about service providers. They said: “The [captive financial] exam process is revealing a range in the quality of work that is quite enlightening. We have worked with several service providers who have provided less-than-satisfactory work product by actively communicating our expectations of them to improve their work.”

Another regulator added: “For already-licensed managers, we review their compliance during exams.” Again, it begins with captive regulation, but naturally leads to proactive service provider regulation.

The process
Concern over the lack of statutory authority or a specific process for removing a captive service provider from an approved list was another common thread among regulators. Some of their comments included:

- “Interesting timing of your question, as we are beginning to discuss related processes and procedures”
- “We have an approval process for captive managers, auditors, and actuaries. We reserve the right to remove them from our approved list. We do not have a formalised process for removing them. It is really based on common sense and the facts and circumstances of what produced the concern”
- “[A Court ruling] is a harder question. I’d like to think that I would be hard-nosed about it; however, without statutory authority, I might be prevented”
- “Although we don’t license captive managers, we would take them from our approved list”

In discussing captive service provider oversight processes, one regulator cited the interaction between insurance departments and other regulatory authorities, saying: “One reason for terminating a captive manager is problems with another licensing agency. For example, a couple of years ago we denied a captive manager application when an attorney, who had [their] law licence suspended, sought to become a manager. We denied the application.” They added: “Additionally, if they are a licensed professional, such as a lawyer, CPA, SEC registration or Finra designations, we have taken action when these other [governing] regulatory bodies do so.”

The future
Where might all of this lead? Expanded regulatory oversight and stricter licensing of captive service providers are real possibilities. One regulator provided some perspective on where captive manager regulation could be headed. “Because of the IRS’ position that many managers of 831(b) captives are promoters, I am hearing discussion about managers [being required to] become licensed producers/agents. This would give states the authority to take action against managers under the existing producer licensing laws.”

This idea tends to split the captive industry between larger managers, most of whom are already licensed producers, and smaller operations that are not. That regulator went on to say: “The NAIC Model Producer Licensing Act, which has been adopted in all states, says that if a person solicits, sells, or negotiates insurance, then a licence is necessary.”

This may already suggest some mandate for expanded captive manager licensing. The reinsurance transactions common in many small captive structures may also suggest a need for licensing.

As the regulator stated: “Additionally, in all states when acting as a reinsurance intermediary, it requires a reinsurance intermediary licence. As you know, many managers place reinsurance coverage. However, a reinsurance intermediary licence is unnecessary if the intermediary is a licensed producer.”

From my perspective as a captive service provider, sometimes regulatory actuary, and periodic captive spokesperson, the ongoing interactions between captive regulators and their service providers are an important conduit through which the industry fosters continuous improvement.

Captive industry members have a vested interest in maintaining high standards for service providers and raising the bar when best practices change. This encourages high-quality service to the captive owners, insureds and regulators we serve, and it strengthens the captive insurance industry’s reputation.